Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of Accounting Standards Under the Telecommunications Act of 1996 Section 272(d) Biennial Audit Procedures	CC Docket No. 96-150

PETITION FOR RECONSIDERATION AND REQUEST FOR STAY

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I. Introduction and Summary.

Pursuant to section 1.106 of the Commission's rules, Verizon Communications Inc. ("Verizon") hereby petitions for reconsideration of the Commission's January 10, 2002 order denying Verizon's request for confidential treatment of information contained in PriceWaterhouseCooper's first biennial section 272(d) audit report of Verizon.[1] The order sets a bad precedent that will impair the conduct of future audits. If the Commission releases these data, it should adopt a protective order to prevent use of the data for purposes other than for commenting on the audit results. Because release of the proprietary information in the audit report will cause Verizon to suffer irreparable competitive harm, Verizon requests a stay of the order pending reconsideration.

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[1] *Accounting Safeguards Under the Telecommunications Act of 1996: Section 272(d) Biennial Audit Procedures*, CC Docket No. 96-150, Memorandum Opinion and Order, FCC 02-1 (rel. Jan. 10, 2002) ("*Order*").

II. The Commission's Decision To Disclose Verizon's Confidential Data Sets A Bad Precedent.

This case marks an unfortunate departure from the Commission's consistent policy of protecting confidential data that it examines in an audit. It will set a bad precedent that will impair future audits and make the audits themselves potential sources of harm to the companies that participate in them.

The Commission has a longstanding policy of protecting the confidentiality of data in an audit, and the Courts have rejected *ad hoc* departures from this policy. ***See*** *Examination of Current Policy Concerning the Treatment of Confidential Information Submitted to the Commission*, Report and Order, 13 FCC Rcd 24816, ¶ 54 (1998); *Qwest v. FCC*, 229 F.3d 1172 (D.C. Cir. 2000). The Commission explained that "[t]his policy is also designed to enhance the efficiency and integrity of our audit process by encouraging carriers to comply in good faith with Commission requests for information." Id. Although carriers are required by statute to make their records available to the Commission, the Commission has found that compelled disclosure of information produced by audits would create a significant risk that the value of the information would decrease;

> the audit process depends largely on the cooperation of carriers who have generally been willing, upon Commission request, to permit examination of existing documents, create new documents and allow employee interviews in the belief that such information will not be disclosed. The Bureau emphasized that the audit process typically involves open-ended topical inquiries that leave carriers with significant room for interpretation, and therefore cooperation of carriers is essential to an efficient and productive audit. If raw data submitted by carriers is disclosed, it is likely that such voluntary assistance will diminish, especially since the audit process does not present the expectation of a government-bestowed benefit. As a result, the Commission will be forced to rely on compulsory measures, which entails a significant risk that the amount and quality of information made available to Commission auditors will be reduced.[2]

[2] *Scott J. Rafferty*, 5 FCC Rcd 4138, ¶ 5 (1990).

Consequently, the Commission found that information gathered in an audit is exempt from disclosure under the Freedom of Information Act under the first prong of the Exemption 4 – that disclosure is likely to "impair the Government's ability to obtain necessary information in the future." ***See*** id. at n.3; *National Parks & Conservation Ass'n v. Morton*, 498 F.2d 765, 770 (D.C. Cir. 1974).

Initially, the Common Carrier Bureau adhered to this policy in conducting the section 272 biennial audit. The Bureau audit staff, the Bell Operating Companies ("BOCs"), and the independent auditing firms worked together to develop procedures for section 272 audits which, since the first release of the procedures in 1998, provided that the audit report would be submitted in draft form to the BOC and that "[t]he Oversight Team will negotiate with the BOC and delete from the final report information deemed to be proprietary."[3] Trusting in those procedures as well as in the Commission's firm policy of protecting audit information and in the independent auditor's professional obligation to keep audit information confidential, Verizon cooperated fully with the auditors and provided all information requested.

In the last month of the audit period, after which most of the data gathering had been completed, the Bureau proposed to modify the agreed-upon procedures to eliminate Verizon's ability to exclude confidential information from the audit, and to replace it with a procedure under which Verizon would redact any information that it considered confidential and submit a request under section 0.459 of the Commission's rules that this information not be available for public inspection. In addition, the Bureau proposed a change in procedures that would require

[3] ***See*** General Standard Procedures for Biennial Audits Required Under Section 272 of the Communications Act of 1934, as Amended, Draft December 16, 1998, ¶ 30(e).

the auditor to include in the public report all information in the workpapers where the agreed-upon procedures required the auditor to "document, describe, identify, list, and note" Verizon's information. Such changes in agreed-upon procedures require the consent of all "users," which includes Verizon. ***See*** id., ¶ 2. Although Verizon never agreed to these changes, the Bureau insisted that the independent auditors follow them. When the independent auditors submitted the first draft of the audit report to the Bureau for its comments pursuant to the Commission's rules, the Bureau instructed the auditors to modify it to include additional detailed information, most of which is confidential. Consequently, Verizon had no choice but to follow the Bureau's proposed procedural changes and redact the confidential information together with a request to withhold the redacted information from public disclosure pursuant to Exemption 4 of the Freedom of Information Act.

The *Order* sets an extremely bad precedent that will impair the Commission's ability to conduct audits in the future. The Order rejects Verizon's request for confidential treatment in its entirety and states that the section 272 biennial audits will not adhere to the Commission's longstanding policy of protecting confidential information from public disclosure. ***See*** *Order*, ¶¶ 8-9. In addition, the order states that the Commission expects to modify the procedures for the information that will be included in the audit report. ***See*** *Order*, n. 18. Consequently, any carrier participating in a section 272 audit in the future will have no way of knowing what confidential information it makes available to the auditor will be put into the public domain at the conclusion of the audit. The carrier will view the auditor as a limitless source for leaking the carrier's confidential information to its competitors. Since the carrier will have no control, or even influence, over the confidential information that will be released, the carrier will not be able to

judge how much competitive harm will result from cooperating with the auditor's request for information. This cannot help but have a chilling effect on future audits.

This undesirable result is completely avoidable. Section 272 provides that the Commission and the state commissions will have full access to the audit workpapers for purposes of assessing a carrier's compliance with the section 272 safeguards. The public report can include the results of the audit without disclosing any confidential information, as was initially provided in the agreed-upon procedures.

The Commission's finding that the section 220(f) requirement that the Commission's staff keep audit information confidential is not applicable to the section 272 biennial audit makes no sense. ***See*** *Order*, ¶ 9. Section 220(c) gives the Commission general authority to examine the books and records of common carriers in both audits and in other proceedings, including section 272 biennial audits, which the *Order* recognizes are more specific applications of the Commission's general auditing power. Section 220(f) imposes a general confidentiality obligation on the Commission's staff regarding any information that the staff receives pursuant to the Commission's authority to examine the carriers' records, whether in an audit under section 220(c) or otherwise. Therefore, this general restriction applies as well to information that the Commission's staff examines during the section 272 audit proceedings. Congress would not have enacted section 272(d)(3)(C), which requires any state commission that participates in the audit to take measures to protect proprietary data from disclosure, if it wanted the Commission's staff to be completely free to make that same information public. Rather, the only logical conclusion is that Congress enacted this stricture to apply to the state commissions because the Commission was already under an obligation to protect the information.

The Commission should reconsider the *Order* and grant confidential treatment to the information that Verizon redacted from the audit report. If the Commission does not withhold the information from public disclosure, it should require any persons seeking access to the unredacted report to execute the Commission's standard protective agreement.[4] The Commission states that disclosure of this information to the public is necessary to permit meaningful comments on the results of the audit. ***See*** *Order*, ¶ 7. A protective agreement would allow any interested person to examine the confidential data and to provide comments to the Commission while protecting Verizon from use of that information for competitive purposes. There is no reason not to impose a protective agreement in this proceeding, as the Commission has done in numerous other proceedings where a carrier's right to confidentiality must coexist with the right of other parties to comment.

III. Release of The Proprietary Data Would Cause Verizon Competitive Harm.

Verizon submitted the audit report together with a request that information marked as "proprietary" on a redacted version of the report be withheld from public disclosure. The Commission denied the request, in part, because it found that these data either are required to be disclosed under the Commission's rules, are disclosed at an aggregate level, are required to be disclosed to evaluate Verizon's compliance with the section 272 rules, or are data whose disclosure would not cause Verizon competitive harm. ***See*** *Order*, ¶¶ 13-20. In fact, all of these observations are either incorrect or irrelevant. Verizon demonstrated that these data are

[4] Even AT&T, which was the first to request access to the confidential information, concedes that it would be reasonable for the Commission to require execution of a protective agreement. ***See*** Letter from Aryeh S. Friedman to Hugh L. Boyle (Aug. 7, 2001).

competitively sensitive and should be withheld from public disclosure under section 0.459 of the Commission's rules and Exemption 4 of the Freedom of Information Act, 5. U.S.C. § 0.552(b)(4).

First, none of these data are required to be disclosed under the Commission's rules. If they were, the Commission would have found that they were not confidential in the first place, and the Commission never makes that finding. For instance, the Commission states that its rules "already require Verizon to publicly disclose information concerning the goods and services a BOC's section 272 affiliate buys from the BOC." *Order*, ¶ 16. However, the rules only require Verizon to post the contracts on its web site and to record the total number of affiliate transactions in its ARMIS reports. They do not require Verizon to disclose the specific quantities of services that the section 272 affiliate ultimately purchases, such as the data in Tables 14a, 14b, and 14c concerning the number of special access circuits that the section 272 affiliates purchased each month.[5] The numbers of presubscribed interexchange carrier ("PIC") change orders in Table 14c reveal how many long distance order changes Verizon's section 272 affiliate submitted in its files each month compared to the total orders for non-affiliated carriers. The Verizon local exchange carrier keeps these types of carrier-specific data confidential for *all* of its customers, including its section 272 affiliates.

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[5] Similarly, the Commission states that the performance data in the section 272 audit report is the type of data publicly disclosed in the carrier-to-carrier performance plan pursuant to the conditions on the GTE/Bell Atlantic merger. ***See*** *Order*, ¶ 17 & n. 52. However, the data that Verizon publishes pursuant to Condition V of the merger order concerns purchases of resale, interconnection and unbundled network elements, not the purchases of exchange access services by the Verizon long distance affiliates that are listed in Tables 14a, 14b, and 14c. In addition, where the merger conditions require Verizon to report performance data for exchange access services provided specifically to its affiliates, the data are given proprietary treatment. ***See*** *Bell Atlantic/GTE Merger Order*, 15 FCC Rcd 14032, Appendix D, ¶ 53 (2000).

Second, the Commission finds that the "information about the section 272 affiliate's financial position is at an aggregated level . . . ." *Order,* ¶ 16. This is incorrect. For example, the balance sheet data on page 5 of the report is detailed for each section 272 affiliate, and the amounts billed by the local exchange companies on Table Nos. 9, 10 and 11 are by section 272 affiliate, by month, for each type of service purchased. The most extreme example of disaggregated data is the information on Table 12, which lists the prices that Bell Atlantic Network Integration paid for specific pieces of equipment from unaffiliated vendors.

Third, the Commission's statement that these data are "needed to evaluate compliance with the section 272 accounting safeguards" (*Order*, ¶ 16) may be correct, but is inapposite to its conclusion that the data should be released to the public. Congress understood that the auditors would need access to both public and confidential information to evaluate a BOC's compliance with section 272 and provided that both the Commission's staff and the state regulatory commissions (but not the public) would have access to all of the audit working papers and supporting material needed to make that evaluation, subject to protective measures designed to prevent public disclosure of confidential data. ***See*** 47 U.S.C. § 272(d)(3). Since Verizon has provided the data as required by section 272 to the commissions and the auditors, the only question is whether public release of that information should be withheld because it would harm Verizon's competitive position, which it would.

Fourth, the Commission's conclusion that disclosure of these data would not cause Verizon competitive harm is incorrect. Most of these data qualify as confidential carrier information under section 222 of the Act with regard to Verizon's section 272 affiliates. The Commission can be sure that Verizon's long distance competitors would object vigorously if

Verizon tried to publicize similar information about their purchases of exchange access service precisely because it is confidential and because it would give their competitors insights about their financial status, market plans, growth potential, and technical capabilities. The Commission cannot presume that Verizon's competitors keep these data confidential for no reason. Nor should it conclude that Verizon has any less interest in protecting its competitive position.

Tables 9, 10 and 11 disclose monthly charges from the Verizon local exchange carrier to its long distance affiliate for joint marketing activities. By comparing these charges to the unit prices in the posted contracts, competitors could determine the volumes of calls that are handled and the numbers of sales that are made through outbound and inbound sales efforts in the business offices and telemarketing services. This would allow competitors to evaluate the effectiveness of Verizon's sales techniques as compared to their own and to analyze the factors affecting Verizon's ability to penetrate the market. With this knowledge, they could plan counter-strategies and gain a competitive advantage over Verizon in the markets covered by the audit as well as in new markets that Verizon will enter in the future.

Table No. 12 discloses the prices that Bell Atlantic Network Integration pays non-affiliated companies for routers, cabinets, and ethernet modems. One of the primary ways that a business obtains a competitive advantage is by obtaining equipment and supplies at a lower price than its competitors are able to obtain from the same vendors. The Commission's decision not to give Verizon confidential treatment of these data puts all suppliers on notice that any favorable prices they give Verizon may later enter the public domain and hinder their ability to negotiate

with other customers. This inevitably will harm Verizon's ability to obtain the best prices from suppliers.

The information on Tables 14a, 14b, and 14c about the volumes of exchange access services that Verizon's section 272 network affiliate purchased each month as Verizon began offering interLATA services in New York and the delivery dates for these access services can be used by Verizon's competitors to assess how much Verizon relies on its own network facilities and how quickly it gears up its facilities-based services to meet demand as it enters a market. These data do not become "stale" a year later, as the Commission presumes (***see*** *Order*, ¶ 19). They may provide useful insights into Verizon's likely entry into subsequent markets as Verizon obtains section 271 approvals. Moreover, by comparing similar information in subsequent audits, competitors will be able to analyze the success of Verizon's marketing strategies and the development of each market. Similarly, the information on pages 45-47 (Objective X, procedure 5) about Verizon's monthly revenues for retail National Directory Assistance ("NDA") Service, by state, lets Verizon's competitors know the locations of Verizon's most lucrative markets and which ones are growing the fastest. This could help them in targeting their own sales and marketing efforts.

The Commission dismisses Verizon's argument that it does not have access to similar information about its competitors, stating that Verizon is subject to section 272 safeguards and that disclosure is the price of enforcing those safeguards. ***See*** *Order*, ¶ 18. This misses the point. The fact that Verizon's competitors keep these types of data confidential is strong evidence that the information is competitively sensitive. If the Commission required all long distance companies to publicize this information, they would at least be on a level playing field.

The Commission's decision to make Verizon's data public while its competitors can keep it confidential puts it at a clear disadvantage.

For these reasons, the Commission should reconsider its finding that public release of these data would not cause Verizon competitive harm.

IV. The Commission Should Stay the Order Until It Decides Verizon's Petition For Reconsideration.

The Commission should stay the effectiveness of the *Order* until it decides whether to grant this petition for reconsideration. The Commission may stay the effect of an order while it is considering a petition for reconsideration "upon good cause shown." 47 C.F.R. § 1.106(n). In determining whether to grant a stay, the Commission uses the test enunciated in *Virginia Petroleum Jobbers Ass'n v. FPC*, 259 F.2d 921, 925 (D.C. Cir. 1958). The factors to be considered are: (1) the likelihood of success on the merits by the party requesting a stay; (2) irreparable harm in the absence of a stay; (3) no substantial harm to other interested parties if the stay is granted; and (4) the public interest in favor of a stay. ***See, e.g.,*** *Heritage Cablevision, Inc. Petition for Stay of Local Rate Order*, 13 FCC Rcd 22842 (1998). The request here meets all parts of that test.

Verizon has made a substantial demonstration herein that release of the confidential information in the audit will cause Verizon direct and irreparable competitive harm and that it would impair the effectiveness of the section 272 audit process. Once Verizon's competitors have access to the financial, transactional, and demand data in the audit report, they will gain insights into Verizon's operations and purchasing practices that will put Verizon at a disadvantage that will be impossible to repair later if the Commission grants Verizon's petition.

The Commission has already postponed the date for comments on the audit report several times in order to consider the requests for access to the confidential data. No interested party would be harmed if the Commission granted another extension of time for the filing of comments to allow additional time to consider Verizon's petition for reconsideration. A stay would be in the public interest because the unprotected disclosure of Verizon's confidential information would have a negative effect on the conduct of this and subsequent audits.

V. Conclusion

The Commission should stay and then reconsider the *Order* and withhold the information that Verizon identified as confidential from public disclosure. If the Commission decides to release this information, it should require any person requesting it to execute the standard protective agreement.

Respectfully submitted,

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